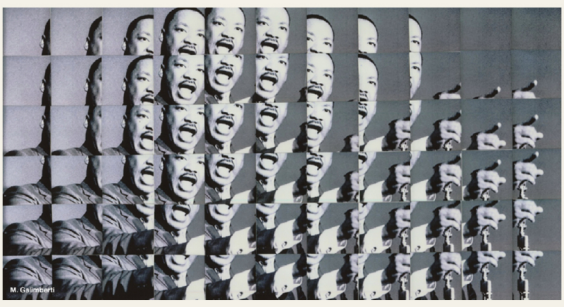

EU AND INTERNATIONAL TAX POLICY

Bonus related to employment activities carried out abroad before becoming Italian resident: a shocking pro-taxpayer ruling may open to tons of refund requests

In 202x, Mr. X was resident in State A and worked as employee in the same State. In 202x+1, Mr. X moved his residence in Italy. In 202x+1, he received part of his compensation for the activities carried on in 202x. Is this compensation taxable in Italy? The answer is yes for the Revenue Agency. It is not for the same Revenue Agency. This is the beauty of the tax world!

The facts

A multinational group of companies implemented a Long-Term Cash Bonus Plan (the "Plan") in favour of its key managers. Some of the beneficiaries are employed by the Italian branch (the "Branch") of a German company (the "Italian Beneficiaries").
The Italian Beneficiaries can in principle be divided into three categories:

i. managers who during the entire vesting period of the Plan have always been employed by the Branch, irrespective of their tax residence;
ii. managers who during the vesting period of the Plan were Italian resident but worked outside Italy;
iii. managers who during the vesting period of the Plan were non-Italian resident and worked outside Italy for the same legal entity (e.g. head office) or for other group companies.

The applicant was concerned about the withholding tax obligations for the Branch arising from the payment of the bonus (the "Bonus") in situations under (iii) with respect to the portion of such Bonus related to vesting periods during which the Italian Beneficiaries were resident outside Italy and worked exclusively abroad.

Year 1	Year 2	Year 3	Year 4
Resident abroad Working abroad Vesting 1/3	Resident abroad Working abroad Vesting 1/3	Resident Italy Working Italy Vesting 1/3	Resident Italy Working Italy Payment of the Bonus

The Italian tax law analysis

The domestic tax law analysis should address two key questions:

- is the Bonus taxable in Italy for the entire amount or just for the portion vested while working in Italy?
- Would the Italian branch act as withholding agent with respect to the entire amount of the Bonus even if the payer is either a different organisation of the same legal entity or a different legal entity?

As for the first question, there is no doubt that the entire amount of the Bonus would be taxable in Italy. Indeed:

i. when the Bonus is paid, the recipients are tax resident of Italy;
ii. Italian tax residents are taxed on worldwide income. Obviously, the portion of the Bonus related to vesting periods during which the recipients were working abroad does qualify as foreign source income and a credit for taxes paid abroad must be granted.

Based on certain reasoning, Italian taxation might be excluded pursuant to Art. 51 (8-bis) CTD but the Revenue Agency's position is that this provision only applies to persons who were resident of Italy while working abroad (this is a highly discriminatory position).
As for the second question, Italian tax authorities have systematically claimed that the employer at the time payment was made should act as withholding agent for the entire amount, irrespective of whether such employer is also the payer of relevant income, provided that all parties belong to the same group of companies. Based on this reasoning, the applicant clarified to have deducted on a prudential basis the withholding tax on the full amount of the Bonus. The position of the applicant is "prudent" also because in a number of rulings tax authorities have taken exactly the same position even though in a number of other rulings, private and not even made public, the position taken by the same authorities was exactly the opposite. Hard to believe. Hard to understand but welcome to real life!

The Ruling: a shocking position

In ruling 81/2025 (the "Ruling"), tax authorities have leveraged not just on Italian domestic tax law but on the applicable treaty (in the case at stake was the Italy/UK Treaty whose relevant Article is aligned to the OECD Model). The position is shocking:

i. Article 15, paragraph 1, of treaties aligned to the OECD Model Treaty states that income from employment activities derived by a resident of a Contracting State is taxable only in this State unless the activity has been carried out in the other Contracting State (subject to the 183-day rule);
ii. since the Italian Beneficiaries in certain years of the vesting period (in the example Years 1 and 2) were resident abroad and worked outside Italy, the relevant income is not taxed in Italy even though actually received when the beneficiary was already resident of Italy;
iii. in practice, Article 15 of the OECD Model Treaty is construed as being applicable on an "accrual basis" rather on a "cash basis" and the expression "income derived" is construed as income that compensates activities of a given year irrespective of the time of payment and therefore even if paid in subsequent years;
iv. based on this reasoning, tax authorities concluded not only that the Branch had no withholding tax obligations on the portion of the Bonus paid in Year 4 and related to Years 1 and 2 but even that this portion of the Bonus is not taxable at all in Italy.

The interpretation of the OECD Model Treaty resulting from the Ruling contradicts a number of official positions stated in circular letters and rulings of tax authorities released in the past and appears very wrong.
Indeed Article 15 states that income from employment activities derived by a resident of a Contracting State is taxed solely in this State unless the activity is carried out in the other State. In this latter case, income is taxable in this other State but not solely in this State.
In addition, even though the Ruling referred to long term bonuses for which a vesting period is set out in the Plan, the same line of reasoning should apply to any items of compensation related to work carried out abroad as a non-resident and paid when the beneficiary is a resident.
For instance:

- in 2024 Mr. X is resident of the UK and works in the UK. As of January 2025 he moves to Italy, the compensation for December is paid in January 2025;
- in 2024 Ms. Y is resident of the UK and works in the UK. As of January 2025 she moves to Italy. Bonus for 2024 is paid in February 2025;
- Mr. X and Ms. Y are resident of the UK for the 2024 and move to Italy in April 2025 becoming Italian tax resident in Italy as of January 2025 (no split year). Income related to January, February and March even if paid before moving to Italy is deemed to be received by Italian residents (an argument can be raised that they were dual resident for the first three months of 2025 and UK residence prevails for treaty purposes but tax authorities have a different positions).

Conclusion

We are used to comment official documents in an objective manner, whether they are pro-Revenue or pro-taxpayers.
The conclusions of the Ruling are manifestly wrong but what is striking is that they contradict decades of official positions of the same authorities on same matters.
Lack of coordination or simply a change in attitude? Probably a pure lack of coordination but if this is true tax authorities should promptly react and take remedy.
In the meanwhile tons of paper for refund requests are under preparation especially for those people who moved to Italy under the impatriate tax regime but not limited to them.

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